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Department of the Treasury

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Date: SEPTEMBER 14, 2009

In Re:

LEGEND:

Trust =

A =

B =

Child C =

Child D =

Child E =

Date 1 =

C Group:

Grandchild C-1 =

Grandchild C-1's Spouse =

Great-grandchild C-1A =

Great-grandchild C-1B =

Great-grandchild C-1C =

D-1 Group:

Grandchild D-1 =

Grandchild D-1's Spouse =

Great-grandchild D-1A =

Great-grandchild D-1B =

D-2 Group:

Grandchild D-2 =

Grandchild D-2's Spouse =

Great-grandchild D-2A =

Great-grandchild D-2B =

Great-grandchild D-2C =

Great-grandchild D-2D =

E-1 Group:

Grandchild E-1 =

Grandchild E-1's Spouse =

Great-grandchild E-1	=
<u>E-2 Group:</u>	
Grandchild E-2	=
Corporate Trustee	=
F	=
G	=
State	=
C Trust	=
D-1 Trust	=
D-2 Trust	=
E-1 Trust	=
E-2 Trust	=
State Statute 1	=
State Statute 2	=

Dear :

This is in response to your submission dated March 17, 2009, concerning the income, gift, estate, and generation-skipping transfer (GST) tax consequences of a proposed division of the Trust.

According to the facts submitted, Trust was created on Date 1, prior to September 25, 1985, by the settlors, A and B (husband and wife), for the primary benefit of their grandchildren and the grandchildren's issue. A and B have three adult children, Child C, Child D, and Child E. Child C has one child, Grandchild C-1. Grandchild C-1, Grandchild C-1's Spouse, and their three children, Great-grandchild C-1A, Great-grandchild C-1B, and Great-grandchild C-1C are referred to as the "C Group."

Child D has two children, Grandchild D-1 and Grandchild D-2. Grandchild D-1, Grandchild D-1's Spouse and their two children, Great-grandchild D-1A and Great-grandchild D-1B are referred to as the "D-1 Group." Grandchild D-2, Grandchild D-2's Spouse and their four children, Great-grandchild D-2A, Great-grandchild D-2B, Great-grandchild D-2C, and Great-grandchild D-2D are referred to as the "D-2 Group."

Child E has two children, Grandchild E-1 and Grandchild E-2. Grandchild E-1, Grandchild E-1's Spouse, and their child, Great-grandchild E-1 are referred to as the "E-1 Group." Grandchild E-2 is referred to as the "E-2 Group."

A and B are both deceased. Child C, Child D, and Child E are still living. The current trustees are Corporate Trustee, and three individuals, F, G, and Grandchild C-1's Spouse (collectively referred to as "the trustee"). The Trust principal has been managed and invested as a single trust, and the distributions of income have been made in equal shares to the five family groups. The pertinent terms of the Trust are as follows.

Section II, paragraph A, provides that if any of Child C, Child D, or Child E are living, the trustee is to distribute the Trust income at least annually to or among settlors' grandchildren, their spouses, and their lineal descendants in such proportions and amounts as the trustee, in its sole discretion, determines. The trustee has the power to

accumulate any portion or all of the income only if the trustee is satisfied that the accumulation of income will be in the best interests of settlors' lineal descendants.

Section II, paragraph A, further provides that, with respect to the principal, the trustee, in its discretion may, at any time or from time to time, distribute any part or all of the principal to or among settlors' grandchildren, their spouses, and their lineal descendants. All distributions of principal are to be at such times and in such proportions and amounts as the trustee determines

Section II, paragraph B, provides that, upon the death of the survivor of Child C, Child D, and Child E, the trustee is to divide the trust into a sufficient number of equal shares so that one share shall be set aside for each then living grandchild of settlors and one share shall be set aside for each deceased grandchild of settlors leaving lineal descendants then living. Each grandchild for whom or for whose lineal descendants a share is set aside shall be referred to as the "Primary Beneficiary" of the trust in which that share is held. The trustee is to hold that share as a separate trust.

Under Section II, paragraph B(1), the trustee shall distribute the income of the separate trust at least annually to or among the primary beneficiary and his or her lineal descendants, and, after the death of the primary beneficiary and all of his or her lineal descendants, to or among settlors' lineal descendants in such proportions as the trustee shall determine in its sole discretion. In lieu of the distribution of income, the trustee shall have the power to accumulate any portion or all of the income of the trust only if the trustee has satisfied itself that such accumulation of income will be in the best interests of the primary beneficiary, his or her lineal descendants, and settlors' lineal descendants.

Under Section II, paragraph B(2), with respect to the principal of the trust, the trustee, in its discretion, may, at any time or from time to time, distribute any part or all of the principal of the trust to or among the primary beneficiary and his or her lineal descendants, and after the death of the primary beneficiary and his or her lineal descendants, to or among settlors' lineal descendants. All distributions shall be at such times and in such proportions and amounts as the trustee shall determine.

Section III provides that, unless sooner terminated, each trust shall end immediately prior to the expiration of twenty-one years from and after the death of the last survivor of settlors and the issue of settlors' parents living on the date of the trust agreement. Thereupon the trustee is to distribute the principal of each such trust outright, in equal shares to the person or persons then entitled to receive the net income thereof, or if there is no person or persons then entitled to receive the net income, to the settlors' heirs, as defined in the trust agreement.

Section IV, paragraph A, provides that if any of the income and/or principal shall be distributable to any beneficiary who has not attained age twenty-one, the trustee shall, until the beneficiary has attained age twenty-one, (1) distribute the income to the beneficiary or the beneficiary's guardian or apply it to the beneficiary's and the

beneficiary's dependents' support, maintenance, education, benefit and/or recreation, as the trustee, in its sole discretion, deems to be to the best interest of the beneficiary and his or her dependents; and (2) postpone distribution of principal to the beneficiary.

Section IV, paragraph B, provides that if at any time, the trustee, in its sole discretion, considers that the funds payable to or for the benefit of a beneficiary, together with the funds available to the beneficiary from other sources, are insufficient to provide properly for the essential needs, such as food, clothing, education, shelter and illness expenses of the beneficiary and his or her dependents, the trustee is authorized to pay or apply so much of the principal in such manner and to such extent as the trustee, in its sole discretion, deems to be necessary to meet the essential needs of the beneficiary and the beneficiary's dependents.

Section VI, paragraph A, provides that any person may add to the trust at any time.

Section VI, paragraph C (4), provides that the number of individual trustees may be increased (not to exceed three) or decreased at any time by a majority of the trustees. Settlers' lineal descendants shall not be eligible to be individual trustees. If, at any time there is no individual trustee, then the number of individual trustees of the size last authorized shall be selected by a majority vote of the competent adult members of the class then eligible to receive distributions or, if none, by a majority vote of such persons, regardless of age or competency. The trustee is to exercise its power to pay income in various proportions and/or accumulate income and its discretionary power to pay principal only upon the majority vote of all trustees. However, if at any time during the administration of the trust or the shares there are no individual trustees, the corporate trustee is authorized to take such action as it, in its sole discretion, deems to be in the best interests of the beneficiaries of the trust or the shares

Section VI, paragraph C(5), provides that an individual trustee may be removed by a majority vote of the other trustees serving or by a majority vote of the competent adult members of the class then eligible to receive distributions, or if none, by a majority vote of such persons, regardless of age or competency.

Section VII, paragraph G, provides that the Trust is to be governed by the laws of State.

It is represented that no additions, constructive or otherwise, have been made to the Trust since either March 1, 1984 (the effective date of § 643(f)) or September 25, 1985.

The trustees have executed an Instrument of Severance (in accordance with State Statute 1) to divide the Trust into five separate, equal, and identical trusts, one trust for each family line described below. Each of the five trusts will be the same in form and terms as the original Trust, except that the beneficiaries of each separate trust will be solely the beneficiaries in the family line for which the separate trust is established. So long as one of the settlers' children, Child C, Child D, and Child E, is surviving, each separate trust is to be administered in accordance with Section II, paragraph A, of the

Trust. Upon the death of the survivor of Child C, Child D, and Child E, each separate trust will be administered in accordance with Section II, paragraph B, of the Trust.

The C Trust will be held for the benefit of the C Group. The D-1 Trust will be held for the benefit of the D-1 Group. The D-2 Trust will be held for the benefit of the D-2 Group. The E-1 Trust will be held for the benefit of the E-1 Group, and the E-2 Trust will be held for the benefit of the E-2 Group.

It is represented that the division will permit the trustee to invest the principal in a manner more particularly suited to each living grandchild and his or her spouse and lineal descendants. The Instrument of Severance will be effective as of the last day of the month in which a favorable private letter ruling is received from the Internal Revenue Service.

You have requested the following rulings:

1. The proposed modification and division of the Trust into five separate and equal trusts, the pro rata transfer of assets from the original Trust to each such separate trust, and the possible change of trustees with respect to any such separate trust will not constitute an addition to or a modification of the Trust (or any of the five separate trusts) that would cause the Trust or any separate trust to lose, wholly or partially, its exempt status under § 2601 of the Internal Revenue Code or § 1433(b)(2)(A) of the Tax Reform Act of 1986 and will not subject distributions from any of the trusts to the generation-skipping transfer tax under Chapter 13.
2. The proposed pro rata distribution of the assets of the Trust to five separate trusts on an equal basis as proposed will not result in the realization of gain or loss to the Trust or to any separate trust or beneficiary thereof under § 61 or § 1001.
3. The proposed division of the Trust and pro rata distribution of assets into five separate trusts will not result in a transfer subject to gift tax under § 2501 by the Trust or by any of the Trust's beneficiaries.
4. The basis of each asset received by each separate trust from Trust will be the same as the basis which that asset maintained when held by the original Trust pursuant to § 1015.
5. The holding period for each asset received by each separate trust from the original Trust will include the same holding period for that asset as held by the original Trust according to § 1223(2).
6. Each of the five separate trusts will constitute a separate trust for purposes of § 643 and for purposes of determining the application of any generation-skipping transfer tax subsequent to the division of the Trust.

Ruling 1

Section 2601 imposes a tax on every generation-skipping transfer (GST), which is

defined under § 2611 as a taxable distribution, a taxable termination, or a direct skip.

Section 1433(b)(2)(A) of the Tax Reform Act of 1986, 1986-3 (Vol. 1) C.B. 1, and § 26.2601-1(b)(1)(i) of the Generation-Skipping Transfer Tax Regulations provide that the generation-skipping transfer tax shall not apply to any generation-skipping transfer under a trust that was irrevocable on September 25, 1985, but only to the extent that such transfer was not made out of corpus added to the trust after September 25, 1985 (or out of income attributable to corpus so added).

Section 26.2601-1(b)(1)(iv) provides that if an addition is made after September 25, 1985, to an irrevocable trust which is excluded from the application of Chapter 13 by reason of § 26.2601-1(b)(1), a pro rata portion of subsequent distributions from (and terminations of interests in property held in) the trust is subject to the provisions of Chapter 13.

Section 26.2601-1(b)(4) provides rules for determining when a modification, judicial construction, settlement agreement, or trustee action with respect to a trust that is exempt from the generation-skipping transfer tax under § 26.2601-1(b)(1), (b)(2), or (b)(3), will not cause the trust to lose its exempt status. The rules of § 26.2601-1(b)(4) are applicable only for purposes of determining whether an exempt trust retains its exempt status for generation-skipping transfer tax purposes. They do not apply in determining, for example, whether the transaction results in a gift subject to gift tax, or may cause the trust to be included in the gross estate of a beneficiary, or may result in the realization of capital gain for purposes of § 1001.

Section 26.2601-1(b)(4)(i)(D) provides that a modification of the governing instrument of an exempt trust by judicial reformation, or nonjudicial reformation that is valid under applicable state law, will not cause an exempt trust to be subject to the provisions of Chapter 13, but only if: 1) the modification does not shift a beneficial interest in the trust to any beneficiary who occupies a lower generation (as defined in § 2651) than the person or persons who held the beneficial interest prior to the modification, and (2) the modification does not extend the time for vesting of any beneficial interest in the trust beyond the period provided for in the original trust. A modification of an exempt trust will result in a shift in a beneficial interest to a lower generation beneficiary if the modification can result in either an increase in the amount of a generation-skipping transfer or the creation of a new generation-skipping transfer.

Section 26.2601-1(b)(4)(i)(E), Example 5, illustrates a situation where a trust that is otherwise exempt from the GST tax is divided into two trusts. Under the facts presented in the example, the division of the Trust into five trusts does not shift any beneficial interest in the trust to a beneficiary who occupies a lower generation (as defined in

§ 2651) than the person or persons who held the beneficial interests prior to the division, and the division does not extend the time for vesting of any beneficial interest in the Trust beyond the period provided for in the original trust.

Under State law, a fiduciary (i.e., a trustee) who is a beneficiary and trustee of a trust that confers on the trustee a power to make discretionary distributions to or for the trustee's personal benefit may exercise that power but shall be limited to distributions for the fiduciary's health, education, support, or maintenance. State Statute 2.

In this case, the Trust was irrevocable on September 25, 1985, and it is represented that no additions to the Trust have been made since September 25, 1985. Based on the facts presented and the representations made, the division of the Trust into the five separate trusts, as described above, will not result in a shift of any beneficial interest in the Trust to any beneficiary who occupies a generation lower than the persons holding the beneficial interests prior to the division. Further, the proposed division will not extend the time for vesting of any beneficial interest in the new trusts beyond the period provided for under the original Trust.

We conclude that the proposed division of the Trust into the C Trust, the D-1 Trust, the D-2 Trust, the E-1 Trust, and the E-2 Trust will not cause the Trust or any of the five divided trusts to lose exempt status under § 1433(b)(2)(A) of the Tax Reform Act of 1986. Accordingly, the Trust and the five divided trusts will not be subject to the provisions of Chapter 13.

Ruling 2

Section 61(a)(3) provides that gross income includes gains derived from dealings in property and, under § 61(a)(15), from an interest in trust.

Section 1001(a) provides that the gain from the sale or other disposition of property is the excess of the amount realized over the adjusted basis provided in § 1011 for determining gain, and the loss is the excess of the adjusted basis provided in § 1011 for determining loss over the amount realized.

Section 1001(b) provides that the amount realized from the sale or other disposition of property shall be the sum of any money received plus the fair market value of the property (other than money) received. Under § 1001(c), except as otherwise provided in subtitle A, the entire amount of gain or loss determined under § 1001(c) on the sale or exchange of property shall be recognized.

Section 1.1001-1(a) of the Income Tax Regulations provides that the gain or loss realized from the conversion of property into cash, or from the exchange of property for other property differing materially either in kind or in extent, is treated as income or loss sustained.

A partition of jointly owned property is not a sale or other disposition of property if the co-owners of the joint property sever their joint interests but do not acquire a new or additional interest as a result of the transaction. Thus, neither gain nor loss is realized on a partition. Rev. Rul. 56-437, 1956-2 C.B. 507.

Cottage Savings Ass'n v. Commissioner, 499 U.S. 554 (1991), considers the issue of

when a sale or exchange has taken place that results in realization of gain or loss under § 1001. In Cottage Savings, a financial institution exchanged its interests in one group of residential mortgage loans for another lender's interests in a different group of residential mortgage loans. The two groups of mortgages were considered "substantially identical" by the agency that regulated the financial institution.

In Cottage Savings, 499 U.S. at 560-61, the Court concluded that § 1.1001-1 reasonably interprets § 1001(a) and stated that an exchange of property gives rise to a realization event under § 1001(a) if the properties exchanged are "materially different." In defining what constitutes a "material difference" for purposes of § 1001(a), the Court stated that properties are "different" in the sense that is "material" to the Code so long as their respective possessors enjoy legal entitlements that are different in kind or extent. Cottage Savings, 499 U.S. at 564-65. The Court held that mortgage loans made to different obligors and secured by different homes did embody distinct legal entitlements, and that the taxpayer realized losses when it exchanged interests in the loans. Cottage Savings, 499 U.S. at 566.

Under State law, a trustee may divide a trust into two or more separate trusts on a fractional basis. See State Statute 1. It is consistent with the Supreme Court's opinion in Cottage Savings to find that the interests of the beneficiaries of the five divided trusts will not differ materially from their interests in the Trust. In the proposed division, the Trust will be divided on a pro rata basis in accordance with state law and under the trustee's powers. Except for the changes described above, the five divided trusts will be administered under the same provisions as the Trust.

Accordingly, the proposed transaction will not result in a material difference in kind or extent of the legal entitlements enjoyed by the beneficiaries, and no gain or loss is realized by the beneficiaries of the Trust on the division for purposes of § 1001(a).

Ruling 3

Section 2501 imposes a tax for each calendar year on the transfer of property by gift during such calendar year by any individual, resident or nonresident.

Section 2511 provides that, subject to certain limitations, the gift tax applies whether the transfer is in trust or otherwise, direct or indirect, and whether the property transferred is real or personal, tangible or intangible.

Section 2512(a) provides that if the gift is made in property, the value thereof at the date of the gift is considered the amount of the gift.

Section 2512(b) provides that where property is transferred for less than an adequate consideration in money or money's worth, then the amount by which the value of the property exceeded the value of the consideration is deemed a gift that is included in computing the amount of gifts made during the calendar year.

The division of the Trust as described above will not result in any change in the beneficial interests of any of the Trust beneficiaries. Accordingly, based on the facts submitted and representations made, the division of the Trust into the C Trust, the D-1 Trust, the D-2 Trust, the E-1 Trust, and the E-2 Trust will not cause any beneficiary of the Trust or of the five separate trusts to have made a taxable gift for federal gift tax purposes under § 2501.

Ruling 4

Section 1015 provides that the basis in property acquired by a transfer in trust is the same as it would be in the hands of the grantor, with adjustments for gain and loss recognized.

Section 1.1015-1(b) provides that property acquired by gift has a single uniform basis although more than one person may acquire an interest in the property. The uniform basis of the property remains fixed subject to proper adjustment for items under §§ 1016 and 1017.

Section 1.1015-2(a)(1) provides that in the case of property acquired after December 31, 1920, by a transfer in trust (other than a transfer in trust by gift, bequest or devise), the basis of property so acquired is the same as it would be in the hands of the grantor increased in the amount of gain or decreased in the amount of loss recognized to the grantor under the law applicable to the year in which the transfer was made.

Section 1.1015-2(a)(2) provides that the principles in § 1.1015-1(b) concerning the uniform basis are applicable in determining basis of property where more than one person acquires an interest in property by transfer in trust.

In this case, because neither § 1001 nor § 61 applies to the proposed transaction, the basis of the assets for each of the C Trust, the D-1 Trust, the D-2 Trust, the E-1 Trust, and the E-2 Trust will be the same as the basis of the assets in the Trust.

Ruling 5

Section 1223(2) provides that, in determining the period for which a taxpayer has held property, however acquired, there is included the period for which the property was held by any other person, if under Chapter 1 of Subtitle A such property has, for the purpose of determining gain or loss from a sale or exchange, the same basis in whole or in part in the taxpayer's hands as it would have in the hands of the other person. See also, § 1.1223-1(b).

We conclude that under § 1223(2) the holding period for each of the C Trust, the D-1 Trust, the D-2 Trust, the E-1 Trust, and the E-2 Trust in each asset received from the Trust will include the respective holding period of the Trust for each such asset.

Ruling 6

Section 643(f) provides that, under regulations to be prescribed by the Secretary, two or more trusts shall be treated as one trust if (1) such trusts have substantially the same grantor or grantors and substantially the same primary beneficiary or beneficiaries, and (2) a principal purpose of such trusts is the avoidance of the tax imposed by Chapter 1 of the Code.

Based on the information submitted and representations made, the five trusts created in accordance with the division of Trust will have the same grantor, but will have different primary beneficiaries, and will be separately managed and administered. Thus, the five trusts will be treated as separate trusts for federal income tax purposes.

Except as specifically ruled upon above, we express no opinion as to the tax consequences of the transaction described above under the cited provisions of the Code or under any other provisions of the Code.

The rulings contained in this letter are based upon information and representations submitted by the taxpayers and accompanied by a penalty of perjury statement executed by an appropriate party. While this office has not verified any of the material submitted in support of the request for rulings, it is subject to verification on examination.

This ruling is directed only to the taxpayers requesting it. Section 6110(k)(3) provides that it may not be used or cited as precedent.

Sincerely,

George Masnik
Chief, Branch 4
Office of the Associate Chief Counsel
(Passthroughs and Special Industries)

Enclosures